No. 9492

IN THE 14

United States Circuit Court of Appeals

For the Ninth Circuit

FRANK A. DOUGHERTY,

Appellant,

vs.

JOHN V. LEWIS, former Collector of Internal Revenue for the First District of California,

Appellee.

APPELLANT'S OPENING BRIEF.

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STATEMENT OF BASIS OF ORIGINAL AND APPELLATE JURISDICTION.

The jurisdiction of the District Court is based upon Section 24, Subdivision 5 of the Judicial Code, as amended (28 U.S.C.A., Section 41, Subdivision 1) giving the District Courts jurisdiction "of all cases arising under any law providing for Internal Revenue". The jurisdiction facts are alleged in the complaint. (R. pp. 1-20.)

The jurisdiction of this Honorable Court is based upon Section 128 of the Judicial Code, as amended (28 U.S.C.A., Section 225, Subdivision (a)), vesting appellate jurisdiction to review final decisions of the

District Courts, in all cases except where a direct review may be had under Section 238 of the Judicial Code, as amended. (28 U.S.C.A., Sec. 345.) The judgment (R. p. 36) denying appellant the relief sought is a final decision.

STATEMENT OF THE CASE.

On May 4, 1938, appellant filed a complaint (R. pp. 1-20) against the former Collector of Internal Revenue for the First District of California, praying the recovery of the sum of $3,557.83, and interest thereon as provided by law, which said sum had been assessed and collected by the former Collector from appellant, for and on account of taxes alleged to be due, under the provisions of Section 3251, Revised Statutes of the United States (26 U.S.C.A., Section 2800, Subdivision (d)), upon distilled spirits produced at a distillery. The complaint alleged the filing with the respondent of a claim for refund of the moneys collected by respondent and the rejection by the Commissioner of Internal Revenue of the Treasury Department of the United States of the claim for refund. (R. p. 4.) The respondent by his answer (R. p. 21) admitted all the allegations of appellant's complaint, save and except the averment contained in paragraphs XII and XIII thereof. The cause was tried by the Court without a jury and on August 8, 1939, the District Court filed a memorandum opinion (R. pp. 22-26) directing judgment for respondent and against appellant.

Findings of fact and conclusions of law were made by the District Court on October 17, 1939 (R. pp. 30-34) and on October 19, 1934 judgment on findings was entered against appellant and in favor of respondent. (R. pp. 35, 36.) Appellant appeals from this judgment. (R. p. 41.)

The sole question for determination by the District Court was, whether under Section 3251, Revised Statutes of the United States (26 U.S.C.A., Section 2800, Subdivision D) the appellant was *such a person* as described in that section, and therefore liable for taxes due on distilled spirits produced at a distillery.

Section 3251 of the Revised Statutes of the United States (26 U.S.C.A., Section 2800, Sub. (d)) provides:

> "Every proprietor or possessor of and every person in any manner interested in the use of, any still, or distilling apparatus, shall be jointly and severally liable for the taxes imposed by law on the distilled spirits produced therefrom."

A SUMMARY OF THE EVIDENCE.

The stenographic reporter's transcript of the evidence taken at the trial below has been designated and included as part of the record on appeal, pursuant to Rules of Civil Procedure, Rule 75.

The evidence adduced at the trial was substantially as follows:

Appellant, in support of his complaint, testified that he was a resident of Monterey County, California, for

20 years prior to the trial and that he farmed a ranch in said county of some 1500 acres. He was not the owner of the ranch but rented the same from one Robert Fatjo; that during October, 1939, he subleased 20 acres of said ranch to certain men; that included in said 20 acres was a barn and two outhouses; that he was to receive as rent the sum of $400.00, or $20.00 an acre a year; that he actually received as rent the sum of $200.00; that he received no other moneys; that on June 3, 1935, he was arrested at his home on the ranch by agents of the Alcohol Tax Agents of the Internal Revenue Department and was taken by them to the barn on the 20 acres he had rented and there saw a still; that until then he had no knowledge of the presence of the still; that he had no interest in the still, that he had invested no money in it; that he was not to receive any of the profits from its operation and that he did not receive any of the profits therefrom; that he was tried on charges concerning the still in question and was by a jury acquitted.

That thereafter the Internal Revenue Department assessed taxes against him and the men found operating the still, on alcohol alleged to have been produced at the still; that thereafter the Collector served a warrant of distraint on the Spreckels Sugar Company, restraining moneys due him and that he paid to the Collector under protest the amount which is the basis of his present suit against the Collector.

On cross-examination he denied knowledge of the existence of the still and any interest therein; that he paid about $2,000.00 rent for the entire farm.

The major portion of his cross-examination is devoted to questions and answers concerning his knowledge of the existence of the still and to whether or not he was receiving an excessive rent. Since the Court below found on conflicting evidence that he had knowledge of the existence of the still and that he did receive excessive rent for his premises, appellant does not on this appeal contest the finding of the trial Court on these questions and therefore, does not summarize the evidence thereon. (R. pp. 50-88.)

The respondent called Robert A. Fatjo, the owner of the ranch, who testified he rented the ranch to appellant for the sum of $2,000.00 a year. (R. pp. 88-92.)

Philip S. George, sales manager of the Pacific Gas & Electric Co. at Salinas, who testified concerning certain applications for power, two by the admitted operators of the still during the time the still was in operation and one by appellant after the seizure of the still by the agents of the Internal Revenue Department. (R. pp. 93-106.)

Edward C. Harkins (R. pp. 106-116), Fred L. Myers (R. pp. 117-123), Claude M. Shanks (R. pp. 123-127), all agents of the Alcohol Tax Unit of the Department of Internal Revenue, testified to facts concerning the discovery and seizure of the still in question and the arrest of appellant and the persons actually operating the still.

Guy J. Pedroni (R. pp. 127-141), Jacob J. Bandour (R. pp. 142-149), Herbert Baltz (R. pp. 149-156), testified in effect, that the rental of $400.00 a year for the 20 acres subleased by appellant was excessive.

Julius Bianchini, one of the operators of the illicit still testified that appellant knew the 20 acres was to be used for a still and that appellant was to receive a rental of $125.00 a month and that he paid appellant on three occasions. On cross-examination, he was uncertain as to the times or amounts paid appellant. (R. pp. 156-172.)

Guiseppi Biagi, another of the illicit still operators, testified appellant knew the use to which the leased property was to be put and that appellant was to receive a rental of $125.00 a month. On cross-examination, he testified that he and Bianchini were the proprietors of the still and that appellant had no interest in the still and did not, and was not to receive any profits therefrom, nor was he to assume any losses. (R. pp. 173-187.)

Angelo Rodoni, testified appellant knew the still was to be operated on the 20 acres leased and that the rent was to be $125.00 a month. (R. pp. 187-201.)

Kasper E. Cadle (R. pp. 209-211), Angelo V. Riandi (R. pp. 212-223), James H. Riley (R. pp. 222-227), Coy Swindle (R. pp. 227-231), called as witnesses by appellant in rebuttal testified the rental of $400.00 a year, was not excessive.

SPECIFICATIONS OF ERROR.

I.

The evidence is insufficient as a matter of law to support the judgment in favor of respondent. (Statement of Points on Appeal, R. p. 232.)

II.

The trial Court erred in a matter of law in holding under the evidence that appellant was within the meaning of Section 3251 of the Revised Statutes (Section 2800 (d) of Title 26, United States Code Annotated) a "person interested in the use of the still, distillery and distilling apparatus. (Statement of Points on Appeal, R. p. 232.)

ARGUMENT.

The evidence is insufficient to support the judgment and the trial Court erred in holding appellant liable for the taxes in question.

Appellant will argue both Specifications of Error, under the same heading because the law applicable thereto is the same.

Section 3251 of the Revised Statutes (Section 2800 (d) of Title 26, United States Code Annotated) provides:

> "Every proprietor or possessor of and every person in any manner interested in the use of any still, distillery or distillery apparatus shall be jointly and severally liable for the taxes imposed by law on the distilled spirits produced therefrom."

That appellant was not a "proprietor or possessor", within the meaning of the statute is conceded by the conclusions of law of the trial Court wherein the Court held "plaintiff was a person interested in the use of

the still, distillery and distilling apparatus. (R. pp. 33-34.)

The only question, in the opinion of appellant, to be here determined is whether on the evidence appellant was "a *person interested in the use of any still*", etc.

A great amount of the evidence is devoted to the question of appellant's knowledge concerning the operation of the illicit still in question and concerning whether or not he received an excessive rent for the premises leased by him. Appellant takes the position his knowledge of the operation of an *illicit* still is immaterial to the question of tax liability because the statute in question taxes the distilled spirits produced from any still whether *illicit* or *licensed*. Appellant here, therefore, makes no point concerning his lack of knowledge. Appellant likewise takes the position that the question of whether or not the rental received was excessive is likewise immaterial. We are not here concerned with any criminal responsibility of appellant. He has had his day in Court on that issue and was absolved by a jury of his peers. We are here concerned solely with a *"revenue measure"* or a "taxing statute".

The provisions of the statute were adopted solely to secure to the Government the payment of the taxes imposed by law on distilled spirits. The tax is payable to the Government whether the spirits were produced legally or illegally.

United States v. Ulrice, 111 U.S. 38, 4 S. Ct. 288;

Colletti v. Cassidy, 12 Fed. Sup. 21;
United States v. Van Slyke, Vol. 28, Fed. Cases, No. 16610.

Taxing statutes in case of doubt are to be construed in favor of the taxpayer.

In connection with an interpretation to be given the statute in question, the Court should take into consideration that if there is any doubt concerning the liability of the appellant herein for the tax due on the distilled spirits produced on the premises he rented, that doubt should be resolved in favor of the appellant and against the Government.

In *Gould v. Gould,* 245 U.S. 151, 38 S. Ct. 53, the Supreme Court said:

> "In the interpretation of statutes levying taxes, it is the established rule not to extend the provisions by implication beyond the clear import of the language used or to enlarge their operation so as to embrace matters not specifically pointed out. In case of doubt, they are construed most strongly against the Government and in favor of the citizen."

The rule quoted above was again approved by the Supreme Court in *United States v. Merriam,* 264 U.S. 179, 44 S. Ct. 69 at 71.

WHO IS "A PERSON IN ANY MANNER INTERESTED IN"?

It is the position of appellant that a landlord or a lessor is not a "person in any manner interested in" within the meaning of the statute in question.

Under the doctrine of *ejusdem generis,* where general words follow the enumeration of particular classes of persons or things, the general words will be construed as applicable only to persons or things of the same nature or class as those enumerated.

59 *Corpus Juris,* 981, Sec. 581.

The statute with which we are concerned, by its language, makes liable for the tax in question "every proprietor or possessor of and every person in any manner interested in the use of". Thus, we contend the particular class of persons liable for the tax by virtue of the statute are "proprietors or possessors of" and then follow the general words "every person in any manner interested in the use of". Thus under the doctrine of *"ejusdem generis"* "every person in any manner interested in the use of" refers back to "proprietor or possessor of", so that to be liable for the tax involved, a person must be a proprietor or possessor of or have an *interest in the losses or profits, and the successes or failures of the business in question or stand in the relation of a partner or shareholder.* It must be conceded by the respondent, for he did not contend in the trial Court, nor did the trial Court find, that appellant was "a proprietor or possessor of" as defined in the statute.

What does the word "interest" mean? It is defined in Webster's New International Dictionary as a "right, title, share or participation in advance, profit and responsibility, as an interest in a brewery".

Is the rent received by a landlord such an "interest"? We respectfully submit that it is not.

Counsel for appellant has been able to find only one case in point construing the statute in question and the construction there given conforms to the contention made on this appeal. In *United States v. Van Slyke,* supra, the facts were substantially as follows:

The Government sued Van Slyke to recover the taxes alleged by the Government to be due on illicit distilled spirits produced at a licensed distillery. The facts showed that one Rogers and one Bunker had the immediate control and management of the business of the distillery, that Van Slyke was the owner of the property. The property had previously been owned by a person named Lentz and that the distillery business had previously been conducted by Lentz and Rogers, that Van Slyke as president of the bank advanced money to Lentz and Rogers and discounted their paper, that to secure these advances Van Slyke took a mortgage on the distillery premises from Lentz, that subsequently this mortgage was foreclosed and the premises bid in by Van Slyke; that subsequently Van Slyke leased the premises to Rogers; that thereafter distilled spirits were produced at the distillery. Thereafter, Rogers and Bunker manufactured illicit wines and spirits which they removed from the distillery and rectified without payment of the tax. That subsequently the distillery and the property where seized and forfeited to the Government. It was the contention of the Government that Van Slyke was liable for the tax because he was the owner and proprietor of the distillery premises and was interested in the profits of the distillery because of the moneys

he had advanced to the persons operating the distillery. The suit was tried before a jury and the Court in instructing the jury said:

> "The defendant admits and the evidence shows that he was the owner of the premises on which the distillery was situated, but he denies that he was the proprietor in the sense in which that word is used in the statute and denies that he had any interest in the use of the still. * * * I think the word 'proprietor' is used in the statute in the sense of an owner who whether in personal possession or not has the exclusive right to and the control over the premises. A person in possession of the premises as lessee under a lease for years, has himself, as against the general owner and all the world, the right to the exclusive possession, control and management of the same during the continuance of the lease, and is for all such purposes as much the proprietor of the premises, for the time being, as though he held the legal title in fee. And I think it was never the intention of the law to make the general owner of premises so leased, and not himself having any right to the possession, control or management of the premises or business carried on, and having no interest in the distillery business except to receive his stipulated rent, liable for the payment of the taxes imposed by the government on the spirits distilled."

The evidence of both appellant and respondent in this case conclusively showed that the appellant herein was not interested in the profits or losses of the distillery business conducted on the premises in question.

He was to receive nothing except the rent for the premises he had leased. He did not in any manner participate in the business there conducted. The evidence does not show that at any time while the distillery was on these premises that the appellant was ever upon the premises or that he in any manner had possession or control thereof or of the business therein conducted.

It was said in *United States v. Van Slyke,* supra:

> "But it would be necessary to go further and show that he had an interest in the distillery business itself."

The facts in the *Van Slyke* case show Van Slyke not only was interested in receiving his rents, but also was interested in collecting the debt due him for moneys he had advanced to the operators of the distillery, whereas, in this case, the evidence shows that the only interest of the appellant was in the collection of his stipulated rent.

The question of whether appellant had knowledge that the still was being illegally operated on his premises is immaterial on the question of his liability for the payment of the tax. We are not here dealing with the question of whether or not the appellant was criminally liable for the operation of an illicit distillery on his premises. We are dealing merely with the construction of a taxing statute and in this connection, it was said in *United States v. Van Slyke,* supra:

> "Again, the jury will understand that the defendant's liability to the payment of the tax, turns

upon the question of his being a proprietor or possessor of the still, or interested in the use of the still, and not upon the question of his knowledge or want of knowledge, as to how the distillery was being run, whether 'straight' or 'crooked'. So that the fact of defendant's having notice that illicit wines were being made by Rogers at the distillery would not make him liable for the tax, if all the interest he had in the success of the business was to collect the debt due the bank for rent and for moneys advanced."

In *Doyle v. Scott, et al.* (Tex. Civ. A.), 134 S. W. 829, the following situation was presented to the Court of Appeals of Texas: Appellant sued as a private citizen and property owner to enjoin one Barfield and one Scott from engaging in selling spirituous liquors, etc., at retail in certain retail premises located in a hotel in Fort Worth, Texas. The Texas law provided that each person, where one or more desire to obtain a liquor dealers license, must state his name in the application therefor and swear "that no other person or corporation is in any manner interested in or to be interested in the proposed business". The evidence showed that the particular saloon in question was operated by Barfield and that the application for the license had been signed by Barfield alone and the license issued to Barfield alone. The premises where the saloon was operated by Barfield was owned by one Scott. The evidence showed that Scott received the sum of $150.00 a month rent and that after all expense had been paid and after Barfield had received a draw-

ing account of $100.00 a month, the profits over and above were divided equally between Barfield, the operator of the saloon, and Scott, the owner of the premises. It was the contention of the appellants in these proceedings, because of this arrangement Scott was a person interested in the business.

The Court said:

> "This state of facts does not constitute Scott a partner or 'in any manner interested in' the business within the meaning of the law cited. *The 'interest' meant by the law means something more than the general interest every landlord has to receive the desired rentals for the use of his property. It must mean some interest in the business itself.* A quotation from Parsons on Partnership may be looked to in illustration. He says: 'Where the owner of property leases it for business purposes, agreeing to receive in rent a proportion of the profits of the business, he receives the amount merely as rent and not as a partner in the business.' "

In *Doyle v. Scott,* supra, the landlord was to receive not only his stipulated rent, but over and above, *was to share equally in the profits of the business,* after allowing the owner a drawing account of $100.00 a month.

In the present case appellant, according to the testimony of the witnesses for both sides, was to receive nothing but his rent. It was not to share in the profits or losses. Under the ruling in *Doyle v. Scott,* supra, the fact that appellant's rent was excessive

would not, make him "a person in any manner interested in the use of any still, etc."

In construing who are persons interested in the use of a still or distillery, the Supreme Court of the State of California has held in *Ricter v. Henningsen,* 110 Cal. 530, that where a corporation was engaged in the business of distilling that a stockholder of the corporation was a person "interested in the use of the still, etc., owned by the corporation and used in its business within the meaning of the statute here under consideration".

The Court there said:

> "A stockholder in a private corporation for profit is not in any proper sense the owner of the property of the corporation as such. He has, however, a direct interest in the corporation. In Plimpton v. Bigelow, 93 N.Y. 591, it was said: 'The owner, being a shareholder in a corporation, has by reason of his ownership of shares, a right to participate according to the amount of his stock in the surplus profits of the corporation on a division and ultimately on its dissolution in the assets remaining after payment of its debts."

The above cited case is authority for the position of appellant that to be a person liable for the tax herein in question, he must have had an interest in the profits or losses, in the success or failure of the still in question.

We submit under the authorities cited that the rent received by a landlord for premises where a still is operated, does not render the landlord a person in

"any manner interested in the use of a still, etc." within the meaning of the statute under discussion. This is true whether the rent be excessive or not. He received nothing but his stipulated rent. This he receives whether the still makes money or loses money. He has no other interest in the still.

CONCLUSION.

We, therefore, respectfully submit the judgment of the District Court should be reversed because,

I. The evidence is insufficient as a matter of law to support the judgment in favor of respondent.

II. The trial Court erred in a matter of law in holding under the evidence that appellant was, within the meaning of Section 3251 of the Revised Statutes (Section 2800 (d) of Title 26, United States Code Annotated) "a person interested in the use of the still, distillery or distilling apparatus".

Dated, San Francisco,
June 10, 1940.

Respectfully submitted,
FAULKNER & O'CONNOR,
Attorneys for Appellant.